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SUBJECT: PROCTOR AND GAMBLE GROUNDBREAKING CEREMONY;
AMBASSADOR MEETS KEY KARACHI OFFICIALS

11. (SBU) SUMMARY: Ambassador Patterson traveled to Pakistan's largest city, Karachi, to attend the groundbreaking of a new Proctor and Gamble (P&G) factory in Port Qasim with Karachi Consul General on December 18. P&G will hire 700 new employees to work in the plant and estimates it may help to create up to 7,000 jobs. Separately, the Ambassador met Adnan Afridi, Managing Director of the Karachi Stock Exchange (KSE), who provided a frank assessment of Pakistan's troubled stock markets. The KSE dropped 13% in its first three days of trading since the removal of the market floor imposed on August 28. Afridi predicted a continued decline of an additional 30%-40% in Pakistan's stock exchange but believes the market will recover after a painful correction. Sindh Governor Dr. Ishrat ul Ebad Khan received the Ambassador and CG at the Governor's House and spoke to U.S. concerns about recent ethnic violence in Karachi. The Ambassador also met Chief Minister Syed Qaim Ali Shah and discussed Pakistan's continuing economic problems. End Summary.

Karachi's Beleaguered Stock Exchange

12. (SBU) The Ambassador's meeting with KSE Director Afridi took place at the Consul General's Residence because of Afridi's concern about security. He was worried the lifting of the floor on KSE stock prices earlier in the week might result in violence by irate investors. Earlier this year, there was a riot of money-losing investors in Karachi's financial district following a stock market plunge. Afridi also told the Ambassador that Karachi's financial district is on high alert because of November's Mumbai attacks.

13. (SBU) Afridi described a variety of problems facing the market including a lawsuit against the KSE, a loss of public faith in the Government of Pakistan (GOP) due to its wavering stance on helping the markets, and fading investor confidence. Afridi, who studied economics and law at Harvard, however, remains a strong believer in free markets. The lawsuit was brought against the management of KSE, the Security and Exchange Commission of Pakistan (SECP), and the National Clearing Company by a group of brokers seeking payment on margin accounts. Afridi estimates that 70-80% of the stock market investment in Pakistan comes from margin accounts. Unlike in the U.S. where brokers fund margin accounts, in Pakistan the

borrowing is done through a third party. With the sharp drop in Pakistan stock prices, many investors are unable to cover their margin calls and the brokers are seeking payments from the lenders to cover losses in margin accounts. The courts have frozen the accounts named in the law suits and the investors cannot liquidate their accounts. Afridi believes these lawsuits should be settled out of court.

¶4. (SBU) When asked by the Ambassador how the proposed government support fund might work in the stock market, Afridi was not overly optimistic. He bemoaned the government's credibility issue, recounting how when the stock market began its decline in April, the Finance Minister said funds would be made available to support the market. Despite several government proposals involving sums of PKR 20 to PKR 30 billion, no agreement was ever reached. Then when Pakistan began discussions with the International Monetary Fund (IMF) in October, the IMF required that any support to the market would first require consultation with the IMF. Late December 17, the IMF agreed to allow Pakistan to provide PKR 20 billion (USD 250 million) to support the stock market through the purchase of shares of seven state owned or managed enterprises. The government plans to offer the shares to Pakistanis living abroad. Afridi expressed concern that calling the program a "stabilization fund" may raise investor expectations too high. He is also concerned that local banks may not want to get involved in the share purchase program. Afridi stated "a lot of mistrust exists between the government and the market." Afridi also thinks the government has become

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too involved in trying to fix all the economy's problems at once. In sum, the government's lack of credibility combined with its perceived interference is scaring off investors.

"Let the Market Forces Happen."

¶5. (SBU) Afridi believes the KSE has been hurt by Morgan Stanley's decision to remove Pakistan from its MSCI index. On December 31, the removal will force many index funds to sell Pakistani shares automatically, further depressing the market since these funds simply invest in the index. He told the Ambassador he had tried unsuccessfully to engage Morgan Stanley on the issue. Afridi blames the media for scaring investors away from the market, especially at the present time when money needs to flow back into the market. He is also concerned about investors who may lose their homes and cars, pledged as collateral for loans to invest in the stock market. He fears this could fuel social unrest. Finally, when asked by the Ambassador if a reasonable recovery was possible, Afridi was cautiously optimistic: "We need to keep people alive for three to six months and then a recovery may happen...We need to let the market forces happen and then there will be a recovery."

Proctor and Gamble Betting on Pakistan's Future

¶6. (SBU) Karachi's Port Qasim Industrial Zone has been under development for the past 15 years and includes 112 ongoing commercial and industrial projects. Other than the DHS cargo scan facility, however, no American firm has located in Port Qasim. Proctor and Gamble's (P&G) decision to locate a plant in Port Qasim is viewed as a vote of confidence in Pakistan's future. P&G plans to begin bulk packaging of diapers at the plant and production of laundry detergent when it is completed in 2010. Initially the production will be marketed in Pakistan but eventually, P&G hopes to use the factory for exports. Laurent Phillipe, P&G's Director for Europe, the Middle East, and Africa pointed out that P&G will only use one-third of the 25 acre site initially.

P&G is optimistic about its future in Pakistan and believes it will need the additional room to expand. He told the Ambassador the plant will initially employ 700 people but he hopes up to 7000 jobs could result in the area as a result of the plant's presence.

¶7. (SBU) Earlier this year, one P&G employee was killed and three were wounded in Hub, Balochistan. P&G is now in the process of shifting their operations from Hub to Port Qasim. P&G had a large turnout of corporate and government leaders including Qaisar Shareef, the Country Manager for P&G and Shaukat Tarin, Advisor to the Prime Minister on Finance, Revenue, and Economic Affairs. In her remarks, Ambassador Patterson called the groundbreaking "a good news day in U.S./Pakistan relations." She noted the plant's potential to provide affordable local products to replace expensive imports and as a place where youth can begin a career in Pakistan. She also called upon the Pakistani Government to lower duty rates on imported materials to help create jobs in Pakistan. In closing she reminded the audience that the U.S. is Pakistan's largest trading partner and foreign investor.

Peace Committees Formed to Ease Tensions

¶8. (SBU) The Ambassador met with Sindh Governor Dr. Israt-ul-Ebad Khan to learn his views on the recent ethnic violence and current situation in Karachi. The Governor acknowledged that local investors are hesitant due to the security situation in the city and opined that Foreign Direct Investment (FDI), such as the P&G investment at Port Qasim lend stability to Pakistan and encourages local investors to remain. Khan acknowledged that the harsh economic situation coupled with ethnic tensions make the

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population susceptible to manipulation by those seeking to foment unrest in the country. He said the demonstrations in October provided a catalyst for the Governor to meet with contacts throughout Karachi society. Peace Committees were established to discuss difficult issues and defuse tensions before they escalate into demonstrations and violence. The Committees, comprised of a mix of sectarian and political representatives, will meet on an on-going basis. "We must have constant dialogue," he noted, "to encourage and ensure reporting of suspicious activities in the communities."

¶9. (SBU) Governor Khan said, "It is the duty of political parties to influence their communities to tolerance," and noted that the ANP appears to have very little actual ground control of the Pashtun community. Khan believes the Pashtuns do not want trouble with their neighbors, but seek only to make an income and live peacefully. "It is not necessarily a fight between ethnic groups," Khan said. The people of Karachi had high hopes for the ANP to represent their constituents as a secular party, but the leadership has proven to be dishearteningly incompetent, Khan opined, adding that the ANP must tackle the issue of ethnic tensions head on.

Inflation is at the Heart of the Food Shortage

¶10. (U) When questioned about the food supply in rural Sindh, the Governor responded that the actual food supply is sufficient for the population. However, food costs have escalated to two or three times the pre-election cost while salaries have remained the same, creating an artificial food shortage. The housing market has gone flat in Pakistan and unemployment has risen, meaning the average family can afford less of the basic necessities. The Governor said he believed it is the combination of economic pressures which make Karachi susceptible to ethnic tensions.

Chief Minister Shah Offers Congratulations on Recent
Presidential Elections

¶11. (SBU) Chief Minister (CM) Syed Qaim Ali Shah offered a congratulatory message to Ambassador Patterson on the outcome of the November presidential election in the United States in a December 18 meeting. CM Shah expressed thanks for the USG's efforts to decrease tensions between Pakistan and India following the Mumbai terrorist attacks. Shah said Pakistan was shocked at the horrible attacks and had great sympathy for India, noting that "Karachi has remained peaceful since this government came into service." Pakistan has followed the USG's recommendation to restrict Jamaat ul-Dawa (JuD) activities, he advised. Twenty-six people have been detained thus far. CM Shah acknowledged the Ambassador's comment that JuD had many charitable elements and said he was confident the government had the capacity to run the schools and hospitals supported by the group, though there were not many such elements in Sindh.

¶12. (SBU) Addressing the law and order situation in Karachi, the CM said that the situation was not tense, but in a city as large as Karachi there will always be concerns. Shah said he believed that the continued emigration into Karachi is evidence that the city is stable. However, Pakistan does need a lot of help with development. The Government of Pakistan (GOP) appreciated U.S. assistance with direct and indirect investment, but needed continued help to tackle unemployment, increase education, and promote good health and hygiene in efforts to eliminate poverty. Under the previous GOP, 1600 schools were closed; those have reopened over the past year; the CM said that the number of girls in school has increased due to incentives offered to families for enrollment, such as scholarships for books and clothing. In 2009, for the first time, a meal will also be offered at school. The

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greatest assistance need for interior Sindh remained disease prevention due to extreme poverty. CM Shah advised that throughout Pakistan there was a dire need for police training and outfitting; the equipment in use was outdated and insufficient to meet the needs of a people under terrorist threat.

¶13. (SBU) Comment: P&G's decision to enter the Pakistan market at a moment when so many investors are withdrawing is an important symbol of U.S. commitment to support Pakistan's economic development. We will look for opportunities to highlight their presence as we work to reinforce our message that U.S. interests in the country transcend the global war on terror.

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